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450 N STREET, SACRAMENTO, CALIFORNIA

(PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0001)

TELEPHONE (916) 324-2655

FAX (916) 323-3387

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January 13, 1998

Jacque D. Wolfe
Attorney at Law
6131 Broadway
Sacramento, California 95820

Dear Mr. Wolfe:

This is in response to your letter of September 7, 1997, to Larry Augusta, Assistant Chief Counsel, Property Taxes, in which you pose three questions concerning the transfer by Olan and Georgia Owsley of their personal residence from their revocable family trust into the Owsley Shelter Trust, an irrevocable inter vivos trust. You ask whether Mr. and Mrs. Owsley retained any beneficial interest in the property and, if so, was that portion subject to reassessment; whether the 1 percent beneficial interest given to Mr. and Mrs. Owsley's daughter, Lois Owsley, in the Owsley Shelter Trust subjects any of the property to reassessment; and whether the Owsley Shelter Trust is a Massachusetts trust/Business Trust, or whether it is an ordinary or traditional trust.

For the reasons set forth in more detail hereinafter, it is our opinion that the Trust is a business trust and that the transfer about which you inquire is a change in ownership under Revenue and Taxation Code section 61, subdivision (j).

In the facts as you have stated them, and on the List of Certificate Holders attached to the Declaration of Trust which you provided, Mr. and Mrs. Owsley, the sole owners and transferors of the residence to the Trust, are specified as, combined, holding a 99% equitable interest in the Trust, and their daughter is specified as holding the remaining 1% interest. Assuming this to be the case for the moment, given the provisions of subdivision (d) (1) of Revenue and Taxation Code section 62, and our view since the enactment of Revenue and Taxation Code section 63.1 that an excluded parent-child transfer may properly be accomplished through the medium of a trust (see Rev. & Tax. Code § 63.1, subd. (c)(9)), it would appear that the more difficult question, and the dispositive one, is your third inquiry: whether this Trust is a business trust or an ordinary trust for the conservation of assets. If it is the former, it has been our long-held position, currently in the process of being incorporated as a part of amendments to Property Tax Rules 462.160, Change in Ownership - Trusts, and 462.180, Change in Ownership - Legal Entities, that it is to be treated as a legal entity for property tax purposes, thereby subject to the provisions of Revenue and Taxation Code sections 61, subdivision (j) and 64. Because the incidence of beneficial interests in the property after the transfer, with Lois Owsley having an interest she did not have previously, is not identical to such incidence prior to the transfer, the exclusion contained

in Section 62, subdivision (a)(2), is not applicable, and the transfer would be a change in ownership, subjecting the entire property to reassessment. On the other hand, if the Trust is characterized as an ordinary (*i. e.*, not business) trust, as noted above, under section 62, subdivision (d)(1), the interest in the property retained by Mr. and Mrs. Owsley would not be considered to have changed ownership, and the transfer of the interest to their daughter, while being a change in ownership, could be excluded for reassessment pursuant to section 63.1.

As you no doubt know, the essential distinction between a business trust, also called a "Massachusetts Trust," and an ordinary or traditional trust is that the former is created for and operated as a business entity, while the latter is created to hold and conserve particular property. See, for example, Revenue and Taxation Code section 23038. The Court in *Koenig v. Johnson* (1945) 71 Cal. App.2d 739, at 749-50, similarly discussed the distinction between business trusts and traditional trusts. See also, Black's Law Dictionary [MASSACHUSETTS TRUST. A business organization wherein property is conveyed to trustees and managed for benefit of holders of certificates like corporate stock certificates.]

Thus, determining whether the Owsley Shelter Trust is a business trust or a traditional trust requires a factual analysis, starting with the evident trust purposes and the trust documents.

The *Koenig* case instructs that the analysis must begin with the trust documents. In the Declaration of Trust which you provided, at Article Twelve, is set forth the "Grantors' Declaration of Purpose." It reads as follows: "TO PROVIDE for the administration of the assets by natural or corporate persons acting in a fiduciary capacity to preserve, conserve, maintain, invest, and develop the assets for the benefit of the certificate holders and in a manner designated in this instrument." (Emphasis added.) Thus, the stated purpose for the trust goes beyond the "holding and conservation of particular property." It includes investing and development as well, more in the nature of conducting business.

Furthermore, a review of the Powers of the Trustees, as set forth in Article Five of the Declaration of Trust, discloses enumerated powers very similar to those of the trust being analyzed by the *Koenig* Court, and which are much more broad than merely to hold, manage, conserve and distribute the trust assets. For example, in this case, as in *Koenig*, the Trustees have the power to buy, sell, lease and invest in property; the power to borrow and to pledge and hypothecate to secure loans; the power to demolish improvements; the power to subdivide; and the power to adjust boundaries. (Section 5.3). They have the power to create servitudes, easements and rights of way, and to seek zoning, rezoning, variance or nonconforming use permits. (Section 5.4) They have the power to buy and sell precious metals and stones (Section 5.5), and to dedicate for public use. (Section 5.6) They have the power to "incorporate, enter into partnerships, associations or other joint ventures..." (Section 5.7), and to invest in stocks and bonds. (Section 5.9) Finally the Trustees have the power "to engage the trust in any business or business activity which is lawfully carried on..." (Section 5.10) These sorts of broad authorized powers were relied upon in part by the *Koenig* Court to find that the trust was a business trust, and "not constituted merely for the purpose of holding and conserving the property of the trustors." See 71 Cal.App.2d at 743, 750. Moreover, the Court held that "the nature of a trust as

a business organization is to be determined from the terms of the trust instrument", and cited with approval a U. S. Supreme Court holding that "The parties are not at liberty to say that their purpose was other or narrower than that which they formally set forth in the instrument under which their activities were conducted." *Id.* Under these rules, we would be compelled to conclude that the Owsley Shelter Trust is a business trust.

One distinction in the *Koenig* case and the cases it relies upon, however, is that in each such case, notwithstanding the language noted above, the court found that the trust was engaged in the conduct of business. We have not been advised of any of the actual activities of the Owsley Shelter Trust, and as such, have no opinion as to whether the Trust has been engaging in business, as the Trustees' powers would enable it to. However, you did advise us that "the only asset which has or can be placed into the trust is the Owsley's personal residence." This is difficult to square with the Declaration of Trust, which references an "Attachment A" as listing all the real property transferred into the trust, and an "Attachment B" as describing "all other property transferred into the trust." Neither an Attachment A nor an Attachment B was included in the materials you supplied, possibly for privacy reasons. (See Section 20.2)

Thus, given the law as discussed above, and the powers of the Trustees as set forth in the Declaration of Trust, if the property is capable of being rented, subdivided, developed, converted to business purposes, or otherwise being used as or in a business, the Owsley Shelter Trust must be considered a business trust and, therefore, a legal entity for property tax purposes.

We offer two further observations. First, irrespective of whether the Trust is determined to be an ordinary trust or a business trust, it is the taxpayers' obligation to establish for the Assessor the relative percentage ownership interests in the property, and to report any changes in ownership. Revenue and Taxation Code sections 480, 480.1. We make this observation because we note that, pursuant to Section 17.1 of the Declaration of Trust, the Trustees are not required to make distributions pro rata to holders of trust certificates. The Trustees may distribute the income or corpus of the Trust to the certificate holders in any percentage they deem necessary for their support, care, maintenance, education, medical expenses or emergencies, presumable even to the exclusion of one or more, in their view, less deserving certificate holders. In addition, the Irrevocable Trust Information Sheet, which may or may not be a part of the Trust document, indicates a distribution of the Trust "shares" which is completely different than you have indicated. Furthermore, Article Ten of the Declaration of Trust appears to authorize distributions to "qualified charitable purposes." Therefore, the actual beneficial or ownership interests may be, as you have indicated and the List of Certificate Holders provides, 99% to Mr. and Mrs. Owsley and 1% to Ms. Lois Owsley, or it may be entirely different. To the extent the actual distribution of the beneficial interests in the property vary from what you report at the present time, a change or changes in ownership may well need to be reported.

Second, irrespective of what transpires in the interim with respect to disputes over the reassessment of the property, a parent-child exclusion is waived if a claim is not filed within the time period specified in subdivision (e) of Revenue and Taxation Code section 63.1. Rev. & Tax. Code § 63.1, subd. (d).

January 13, 1998

The views expressed in this letter are advisory only; they represent the analysis of the legal staff of the Board based on present law and the facts set forth herein, and are not binding on any person or public entity.

Sincerely,



Daniel G. Nauman
Tax Counsel

DGD:jd
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cc: Honorable Bruce Dear
Placer County Assessor

Mr. Richard Johnson, MIC:63
Mr. Rudy Bischof, MIC:64
Ms. Jennifer Willis, MIC:70

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